TAXING INCOMES OF FOREIGN INVESTORS IN AMERICAN STOCKS AND BONDS.

Foreign investors are materially affected by the recent reversal by the Treasury Department of its ruling as to the taxability of incomes of non-resident aliens from bonds and stocks of corporations organized in the United States.

On March 21, 1916, the Commissioner of Internal Revenue ruled as follows:[1]

"Under the decision of the Supreme Court of the United States in the case of Brushaber *v.* Union Pacific Railway Company, decided January 24, 1916, it is hereby held that income accruing to non-resident aliens in the form of interest from the bonds and dividends on the stock of domestic corporations is subject to the income tax imposed by the Act of October 3, 1913."

This ruling expressly repeals a former Treasury Decision, which read as follows:[2]

"Interest on bonds of domestic corporations and dividends on stock of domestic corporations owned by non-resident aliens, and whether such bonds and stock be physically located within or without the United States, are not subject to the income tax."

It also repeals another Treasury Decision, which read as follows:[3]

"Interest from bonds and dividends on stock of domestic corporations, owned by non-resident aliens, are not subject to the income tax, whether such bonds and stock are physically located within or without the United States or whether they are in the possession of agents, or trustees in some fiduciary capacity, in the United States or otherwise."

The first ruling above mentioned states "that it will be held effective as of January 1st, 1916". About two weeks later, however, on April 4th, 1916, the Commissioner rendered a further decision, as follows (T. D. 2317):

"The provisions of Treasury Decision 2313 of March 21st, 1916, relative to withholding the normal tax of 1% at the source on income paid to non-resident aliens from corporate obligations will be held effective as of May 1st, 1916."

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[1] T. D. 2313.
[2] T. D. 2017.
[3] T. D. 2162.

At the request of numerous railroads and security investment houses, the Department held a hearing upon the new ruling on April 18th, 1916, and as a result of the protest there made, the time at which the provision regarding the withholding of the normal tax at the source is to become operative was further extended until July 1st, 1916.

Two interesting questions for the Courts are presented by this new ruling:

I. Is it intended by the Income Tax Law to tax incomes from stocks and bonds held by non-residents?

II. If that is the law's intent, has the United States the power to impose such a tax and if so, to what extent?

I.

The Law's Intent.

The language of the Law pertinent to this discussion is as follows:[4]

"and a like tax shall be assessed, levied, collected, and paid annually upon the entire net income from all property owned and of every business, trade, or profession carried on in the United States by persons residing elsewhere."

The reversing ruling is stated by the Department to be based on the authority of *Brushaber* v. *The Union Pacific R. R.*[5]

Comprehensive as was the decision in that case, the opinion in no way refers to non-resident aliens, the facts of the case did not present the question of the intent of the law or the power to impose a tax on such income, the matter was not referred to in the argument of counsel, and there was no attempt by the Supreme Court, either in this case or in any of the others which have been before it involving the present Income Tax Law, to pass upon those questions.

The original rulings of the Treasury Department that such income was not taxable were based upon two opinions of the Attorney-General addressed to the Treasury Department, one dated October 23rd, 1913,[6] and the other dated July 15th, 1914.[7]

[4] 38 Stat. 166.

[5] (1916) 240 U. S. 1, 36 Sup. Ct. 236.

[6] 30 Op. Atty. Gen. 230.

[7] 30 Op. Atty. Gen. 273.

In the first of these the Attorney General said regarding the taxation of incomes from bonds:

"In substance, you wish to be advised whether, in pursuance of this paragraph (the above quoted sections of the law), the regulations which you are about to promulgate should direct the levying, assessing, and collecting of a tax upon the interest accruing upon bonds executed by a resident or citizen of the United States, whether secured by a mortgage or no, when such bonds are held or owned by a citizen or resident of a foreign country. Also, whether this tax should be levied upon the interest thereon where bonds executed by a non-resident foreigner, and secured by a mortgage on real estate in the United States, are held and owned by another non-resident foreigner.

I am of opinion that the quoted provision does not lay a tax upon the interest accruing on bonds of the character specified when held and owned by a non-resident foreigner, and that this is true irrespective of whether they are unsecured or secured by a mortgage upon real estate in this country, and also irrespective of where the written bonds are in fact kept or interest payments thereon are made."

In the second opinion the Attorney General said regarding the taxation of income from stocks:

"In my opinion, the mere receipt of dividends and income from domestic corporate stock by a non-resident alien, is not a 'business, trade, or profession carried on in the United States.' See *McCoach* v. *Minehill Railroad Co.* (1913), 228 U. S. 295.

"Your question is, therefore, in substance: Are shares of domestic corporate stock owned by non-resident aliens 'property . . . in the United States,' within the meaning of the above statute.

"The fact that property and its situs, in relation to the taxing power, have been frequent subjects of judicial interpretation by Federal and State courts, must be given weight in construing the intention of Congress in using the words above quoted.

"In *Covington* v. *First National Bank of Covington* (1905), 198 U. S. 100, 111, it had been held:

'The situs of shares of foreign-held stock in an incorporated company, in the absence of legislation imposing a duty upon the company to return the stock within the State as the agent of the owner, is at the domicile of the owner. Cooley on Taxation, 16.'

"A similar statement of the law is found in *Hawley* v. *Malden* (1914), 232 U. S. 1, 11, 12 (decided in January, 1914, within three months after the passage of the Income Tax Law):

'While the shareholder's rights are those of a member of the corporation entitled to have the corporate enterprise conducted in accordance with its charter, they are still in the nature

of contract rights or *choses in action*. Morawetz on Corporations, sec. 225. As such, in the absence of legislation prescribing a different rule, they are appropriately related to the person of the owner, and, being held by him at his domicile, constitute property with respect to which he is under obligation to contribute to the support of the Government whose protection he enjoys.'

"The courts having thus defined the situs of corporate stock for purposes of taxation, and a tax upon income being a direct property tax, *Pollock* v. *Farmers Loan & Trust Co.*, 158 U. S. 601 (the XVI Amendment [page 4] merely enlarging the powers of the United States, without changing the legal nature of the tax), it follows that Congress must be deemed to have used the words 'property . . . in the United States' as including only such forms of property as had a legal situs therein. I find in this statute no enactment taxing income from corporate stock in specific terms, and no appropriate language evincing any intention to fix by legislation the situs of such stock.

"The intention of Congress to impose a tax must be expressed in 'clear and unambiguous' language. *United States* v. *Isham* (1873), 17 Wall. 496, 504; *Eidman* v. *Martinez* (1902), 184 U. S. 578, 583; *Benziger* v. *United States* (1904), 192 U. S. 38, 55; *Spreckels Sugar Refining Co.* v. *McClain* (1904), 192 U. S. 397, 416; 23 Op. 62.

"In my opinion, therefore, shares of stock of domestic corporations owned by non-resident aliens are not 'property * * * in the United States' within the meaning of the act of October 3, 1913, and dividends accruing therefrom to such non-resident aliens are not subject to any tax under said act.

"This opinion is confined to a construction of the legal import and intent of the statute in question; and I express no opinion whatever as to the power of Congress, by appropriate legislation, to impose such a tax."

No new opinion from the Attorney General was received or asked for prior to the reversal by the Department of its previous ruling, and if either Mr. McReynolds, who rendered the opinion, or his successor, has changed his mind since the Brushaber case,[8] the change has not been publicly indicated, nor stated to the Treasury Department.

From a logical point of view the Attorney General's opinions are doubtless correct. Bonds and stocks as choses in action undoubtedly have a situs at the domicile of their owner and as property should have but a single location. Unfortunately, however, the courts have not consistently held that the domicil of the owner is their sole situs when questions of taxation are

[8]Brushaber *v.* The Union Pacific R. R. (1916) 240 U. S. 1, 36 Sup. Ct. 236.

involved. The cases which the Attorney General cites hold, it is true, that stocks of a corporation of a particular state have a situs and are taxable at the domicil of a non-resident owner, but they do not hold that they are not property anywhere else. In the case of *Hawley* v. *Malden*,[9] which the Attorney General cites, the opinion specifically indicates that the principle which it announces obtains only "in the absence of legislation prescribing a different rule," and goes on to say:[10]

"Undoubtedly, the State in which a corporation is organized may provide in creating it for the taxation in that State of all of its shares whether owned by residents or non-residents."

As a matter of fact legislation exists in many States which has the effect, according to the construction put upon it and sustained by the United States Supreme Court, of causing stocks of corporations organized in the State to have a situs there, though the owners are non-resident. For instance, the Supreme Court so construed a statute of Maryland in *Corry* v. *Baltimore*,[11] and the court said:

"That it was within the power of the State to fix, for the purposes of taxation, the situs of stock in a domestic corporation, whether held by residents or non-residents, is so conclusively settled by the prior adjudication of this court, that the subject is not open for discussion."

This view is also laid down in *Covington* v. *First National Bank*,[12] *Travellers' Ins. Co.* v. *Conn.*,[13] *Tappan* v. *Merchants' National Bank*.[14]

In view of these decisions it is scarcely safe to conclude that stocks of corporations organized in the United States held by non-resident aliens are not under any circumstances "property" in the United States.

It is equally unsafe to draw such a conclusion regarding foreign held bonds. The Attorney General's opinion regarding these cites no authorities and gives no reasons, but certainly the courts, whether logically or not, have not consistently held that bonds are never "property" at any place other than the owner's domicile.

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[9](1914) 232 U. S. 1, 34 Sup. Ct. 201.
[10]At p. 12.
[11](1905) 196 U. S. 466, 25 Sup. Ct. 297.
[12](1905) 198 U. S. 100, 25 Sup. Ct. 562.
[13](1902) 185 U. S. 364, 22 Sup. Ct. 673.
[14](1873) 86 U. S. 490.

For instance, in *Bristol* v. *Washington County*,[15] bonds of a resident of New York secured by a mortgage on property in Minnesota were held to be taxable in Minnesota where the bonds and mortgages were in the hands of agents in Minnesota.

Again in *New Orleans* v. *Stempel*,[16] certain credits and notes belonging to a resident of New York were held to be taxable in Louisiana under a personal property tax where the evidences of indebtedness were located in Louisiana. A similar holding is found in *Savings, etc. Society* v. *Multnomah County*.[17]

The grounds upon which the Attorney General bases his conclusions that it is not the intent of the law to tax incomes of non-resident aliens from stocks and bonds of American corporations, seem therefore open to criticism. If stocks and bonds under certain circumstances are for taxation purposes viewed as property elsewhere than at the owner's domicile and therefore sometimes as property in the United States, though the owner is a non-resident alien, and the law purports to tax incomes from all property in the United States, then such income would apparently, under those circumstances, come within the intent of the law.

But there are other reasons not given by the Attorney General which may perhaps support in part his conclusions.

It is not to be presumed that the law intends to levy taxes beyond the power of the United States nor beyond its normal jurisdictional scope. The Attorney General says that his opinion extends only to the intent and not to the power of congress. But if his other reasons are insufficient, the extent of the taxing power may be of great importance in determining what the intent is.

II.

Extent of Power to Impose Such a Tax.

In discussing the jurisdictional extent of the power of the United States to impose taxes we are not concerned with any constitutional limitations, because so far as territorial jurisdiction is concerned there are none.

There are, however, certain territorial limits on the power of any nation to impose taxes which have been recognized by

[15] (1900) 177 U. S. 133, 20 Sup. Ct. 585.
[16] (1899) 175 U. S. 309, 20 Sup. Ct. 110.
[17] (1898) 169 U. S. 421, 18 Sup. Ct. 392.

the courts both in this country and in England and which are based on sound principles of comity.

Cooley, in his work on taxation says:[18]

"A state can no more subject to its power a single person or a single article of property whose residence or legal *situs* is in another state, than it can subject all the citizens or all the property of such other state to its power. The accidental circumstances that it may happen to have the means of reaching one and not the rest can make no difference; there must be an interest in the subject matter of the tax; there must be between the state and the tax-payer a reciprocity of duty and obligation, and these, in contemplation of law, would be wholly wanting in the case supposed."

In *State Tax on Foreign Held Bonds*,[19] Judge Field, delivering the opinion of the court, said:

"The power of taxation, however vast in its character and searching in its extent, is necessarily limited to subjects within the jurisdiction of the state. These subjects are persons, property and business."

In *Erie R. R.* v. *Pennsylvania*,[20] the court said:[21]

"No principle is better settled than that the power of a state, even in its power of taxation in respect to property, is limited to such as is within its jurisdiction. *State Tax on Foreign held Bonds*, 15 Wall. 300, 319; *Railroad Co.* v. *Jackson*, 7 Wall. 262; *St. Louis* v. *Ferry Co.*, 11 Wall. 423; *Delaware Railroad Tax*, 18 Wall. 206."

In a dissenting opinion delivered by Justice Field in the case of *U. S.* v. *Erie R. R.*,[22] it is said:[23]

"The power of the United States to tax is limited to persons, property, and business within their jurisdiction as much as that of a state is limited to the same subjects within its jurisdiction."

In the cases of *The Calcutta Jute Mills Co.* v. *Nicholson* and *The Cesena Sulphur Co.* v. *Nicholson*,[24] tried together, Kelly C. B., says:[25]

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[18] Vol. I (3rd ed.) at p. 249.
[19] (1872) 82 U. S. 300.
[20] (1894) 153 U. S. 628, 14 Sup. Ct. 952.
[21] At p. 646.
[22] (1882) 106 U. S. 327, 1 Sup. Ct. 223.
[23] At p. 333.
[24] 35 L. T. R. [N. S.] 275.
[25] At p. 283.

"Before I conclude my observations on this case, I might say that in the first place the great principle of the law of England in relation to taxation is, that the tax shall only be imposed upon persons or things actually within this country."

If there are certain territorial limitations to the jurisdiction of the United States to tax, it becomes important to determine exactly what is taxed by an income tax in order to determine whether the subject of taxation is within that jurisdiction.

The Attorney General says in his opinion above quoted,[26] that an income tax as defined by the Pollock case,[27] is a "direct property tax." The Pollock case does not, however, wholly identify a tax upon the income with a tax upon the property which is the source of the income. It merely held that the income and its source in the case of real and personal property at least are so closely identified that it must have been the intention of the framers of the Constitution to include a tax on income in the same category with the tax upon its source. It is true that in the original hearing,[28] the Chief Justice in referring to a number of cases says that "In none of them is it determined that taxes on rents or income derived from land are not taxes on land;" and also refers,[29] as authorities for the decision, to previous cases holding that "the tax on the occupation of an importer was the same as the tax on imports;" that "a tax on the income of United States securities was a tax on the securities themselves;" that "the income from an official position could not be taxed if the office itself was exempt;" that "the duty on a bill of lading was the same thing as the duty on the article which it represented;" and that "a tax on income received from interstate commerce was a tax upon the commerce itself." However, the opinion nowhere positively states that a tax on income is a tax on the source of the income, and in the re-hearing the Court, referring to the previous decision, says:[30]

"The Court went no farther, as to the tax on the income from real estate than to hold that it fell *within the same class as the source whence the income was derived,* that is, that a tax upon the

[26]30 Op. Atty. Gen. 273.

[27]Pollock *v.* Farmers' Loan & Trust Co. (1895) 158 U. S. 601, 15 Sup. Ct. 912.

[28]Pollock *v.* Farmers' Loan & Trust Co. (1895) 157 U. S. 429, 579, 15 Sup. Ct. 673.

[29]At pp. 581, 582.

[30](1895) 158 U. S. 601, 618, 15 Sup. Ct. 912. The italics are the author's.

realty and a tax upon the receipts therefrom were alike direct, * * * and we are unable to conclude that the enforced subtraction from the yield of all the owner's real or personal property in the manner prescribed, is so different from a tax upon the property itself, that it is not a direct, but an indirect tax, within the meaning of the Constitution."

The opinion of the Supreme Court in the Brushaber case[31] carefully differentiated an income tax as being "direct" in a *"constitutional sense"* from taxes which are direct upon property. The court there in discussing the decision in the Pollock case said:[32]

"While not questioning at all that in common understanding it was *direct merely on income* and *only indirect* on property, it was held that considering the substance of things it was direct on property in a constitutional sense since to burden an income by a tax was from the point of substance to burden the property from which the income was derived and thus accomplish the very thing which the provision as to apportionment of direct taxes was adopted to prevent."

For jurisdictional purposes the Court is not, therefore, precluded by the Pollock case[33] and the Brushaber case from separating the income from its source. If the Act of 1913[34] is construed as taxing income only after it becomes the property of the person to whom it accrues, it may obviously have a different situs from its source, and the jurisdiction of the United States over "income" for taxing purposes may not be coincident with its jurisdiction over the property from which it arises. If the court adopts the view that the income is separable from its source, the court can nevertheless permit the Act to operate wherever it can find *income* as such within the jurisdiction of the United States. It would seem reasonable to tax *incomes* at any place where the income can be found as such, whether it has reached the person to whom it accrues or not. Upon such a basis the place where the income is *payable* may be a determining factor.

Foster, in his work on the Income Tax of 1913, seems to think that the right of taxation of income arising from debts due to

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[31]Brushaber *v.* The Union Pacific R. R. (1916) 240 U. S. 1, 36 Sup. Ct. 236.

[32]At p. 16. The italics are the author's.

[33]Pollock *v.* Farmers' Loan & Trust Co. (1895) 157 U. S. 429, 15 Sup. Ct. 673.

[34]38 Stat. 166.

non-residents by residents of the United States is a closed question. He says:[35]

"Congress may tax all persons within the United States and all property within the United States, whether owned by residents or non-residents, *including debts due by residents of the United States to non-resident* aliens, and may collect from the debtor under a statute authorizing him to deduct the amount of the tax from the sum due his debtor."

In support of the latter part of this statement, Foster relies upon the opinion of Justice Bradley, with whom concurred Justice Harlan, in the case of *U. S.* v. *Erie Ry.*,[36] and quotes from that opinion, as follows:[37]

"I always regarded the tax which, by the one hundred and twenty-second section of the Internal Revenue Act of 1864, was laid upon the interest payable on the bonds and upon the dividends declared on the stock of railroad and other corporations, as a tax on the incomes *pro tanto* of the holders of such bonds and stock. *Stockdale* v. *Insurance Companies,* 20 Wall. 323, 333; *Railroad Company* v. *Rose,* 95 U. S. 78. * * *

"The objection that Congress had no power to tax non-resident aliens is met by the fact that the tax was not assessed against them personally, but against the *rem,* the credit, the debt due *to* them. Congress has the right to tax all property within the jurisdiction of the United States, with certain exceptions not necessary to be noted. In this case, the money due to non-resident bondholders was in the United States—in the hands of the company—before it could be transmitted to London, or other place where the bondholders resided. Whilst here it was liable to taxation. Congress, by the internal revenue law, by way of tax, stopped a part of the money before its transmission, namely, five per cent of it. Plausible grounds for levying such a tax might be assigned. It might be said that the creditor is protected by our laws in the enjoyment of the debt; that the whole machinery of our courts and the physical power of the government are placed at his disposal for its security and collection.

"Whether taxation thus imposed would be respected by foreign governments if the creditor could bring before their courts the debtor company or its property, does not concern us in considering the question now presented. There is nothing in the Constitution which authorizes this court, or any other court, to disaffirm the power of Congress to lay the tax. Congress is its own judge of the propriety or expediency of laying it.

"Indeed, so far as the power of Congress is concerned, regarded in reference to any power the courts have to limit or re-

[35] At pp. 28, 29. The italics are the author's.

[36] (1882) 106 U. S. 327, 1 Sup. Ct. 223.

[37] At p. 703.

strain it, I see no reason why Congress may not lay a tax upon any property on which the government can lay its hands, whether within or without the jurisdiction of the United States. If, in imitation of the dues levied by Denmark upon vessels passing through the Cattegat Sound, Congress should levy a duty upon all vessels passing through the Strait of Florida, I do not know of any power which the courts possess to prevent it. It might create complications with foreign governments, it is true, and involve the country in war; but Congress has the power, if it chooses to take the responsibility, of creating, or giving occasion to such complications. The responsibility rests upon it alone.

"So if, in taxing money due from citizens of the United States to foreign citizens, any complications arise with the governments to which the latter are subject, Congress alone has the responsibility, and is the only department of our government, which has a right to take such a responsibility.

" * * * Considering, therefore, that if Congress chooses to take the responsibility of levying such a tax as the one in question, the courts have no power to control its action, or to give any relief to parties affected by it, I concur in the judgment of reversal."

This opinion is reported in the appendix to the official volume, and does not state the ground upon which the opinion of the court was delivered. The opinion of the court dismissed the case upon the authority of *Railroad Co.* v. *Collector*.[38] That case involved the tax also levied under Section 122 of the internal Revenue Act of 1864 as amended in 1866,[39] and was a suit by the Michigan Central Railroad Company against the Collector of Internal Revenue, to recover back a tax which had been paid to the Collector and retained from bonds paid by the Company in London to non-resident aliens. The railroad Company was not permitted to recover back the tax because the court interpreted the Act as imposing "an excise on the business of the class of corporations mentioned in the statute." The court said:[40]

"* * * the tax was not laid on the bondholders who received the interest, but on the earnings of the corporation which paid the interest."

There were sections in the Internal Revenue Laws passed in 1861, 1862, 1864 and 1866 which imposed taxes upon the incomes of individuals. Section 122 of the Act of 1864, as amended in

[38](1879) 100 U. S. 595.

[39]14 Stat. 138.

[40]100 U. S. at p. 598.

1866, however, was consistently interpreted by the court as imposing a tax not upon the bondholder, but an excise tax upon the corporation measured by sums which it paid out. *In Railroad Company* v. *Rose*,[41] the court said:[42]

"The tax specified in sect. 122 was levied upon railroad, canal, turnpike, canal navigation, and slack-water companies. The section did not include the tax upon the income of individuals. That was provided for always in other separate and distinct sections."[43]

Prior to these decisions the Supreme Court had apparently been somewhat undecided as to whether the section imposed an excise tax on the corporation or a tax on the bondholders.[44]

In view of the latter decisions, that the section imposed only an excise tax on the corporation and not on the bondholder, the opinion of Justice Bradley, relied upon by Foster, evidently misses the point, and the actual decisions under Sec. 122 of the Act of 1864 are, therefore, no authority for upholding the present tax upon the income from bonds held by foreign non-residents.

It is to be noted that Justice Field throughout all the decisions interpreting Section 122 of the Act of 1864, consistently held that the Act did impose a tax upon the income of the bondholder, and when the case of a foreign-held bond was presented in *U. S.* v *Erie Ry.*,[45] he dissented from the decision of the court in a vigorous opinion, upon the ground that the situs of the income was not within the jurisdiction of the United States. He said:[46]

"The bonds, upon the interest of which the tax in this case was laid, are held in Europe, principally in England; they were negotiated there; the principal and interest are payable there; they are held by aliens there, and the interest on them has always been paid there. The money which paid the interest was, until paid, the property of the company; *when it became the property of the bondholders it was outside of the jurisdiction of the United States.* * * * The foreign owner of these bonds was not in any respect subject to the jurisdiction of the United States,

[41](1877) 95 U. S. 78.

[42]At p. 79.

[43]The same principle was upheld in Memphis & Charleston R. R. *v.* United States (1883) 108 U. S. 228, 2 Sup. Ct. 482, and in Bailey *v.* Railroad (1882) 106 U. S. 109, 1 Sup. Ct. 62.

[44]Stockdale *v.* The Insurance Companies (1873) 87 U. S. 323; Railroad Company *v.* Jackson (1868) 74 U. S. 262; United States *v.* Railroad Company (1872) 84 U. S. 322; Haight *v.* Railroad Company (1867) 73 U. S. 15.

[45](1882) 106 U. S. 327, 1 Sup. Ct. 223.

[46]At pp. 332, 333.

neither was this portion of his income. His debtor was, and so was the money of his debtor; but the money of his debtor did not become a part of his income until it was paid to him, and in this case the payment was outside of the United States, in accordance with the obligations of the contract which he held. The power of the United States to tax is limited to persons, property, and business within their jurisdiction as much as that of a State is limited to the same subjects within its jurisdiction. *State Tax on Foreign-Held Bonds,* 15 Wall. 300."

If Section 122 of the Act of 1864 did in fact impose a tax upon the bondholder, as Justice Field, Justice Bradley and Justice Harlan interpreted it, the position of Justice Field seems to be much more in line with the weight of authority than the opinion of Justice Bradley.[47]

In *State Tax on Foreign-Held Bonds,*[48] the Supreme Court held that the State of Pennsylvania could not tax the interest payable on bonds of a railroad company incorporated in the State, held by non-residents. The court said:[49]

"But debts owing by corporations, like debts owing by individuals, are not property of the debtors in any sense; they are obligations of the debtors, and only possess value in the hands of the creditors. With them they are property, and in their hands they may be taxed. To call debts property of the debtors is simply to misuse terms. * * *

"The bonds issued by the railroad company in this case are undoubtedly property, but property in the hands of the holders, not property of the obligors. So far as they are held by non-residents of the State, they are property beyond the jurisdiction of the State."

In *Erie R. R.* v. *Pennsylvania,*[50] the court, interpreting a similar statute in Pennsylvania, held that the Act could not compel a foreign corporation to deduct a Pennsylvania tax from the interest payable in New York upon bonds owned by residents of the State of Pennsylvania, although the corporation had authority to do business in Pennsylvania and said:

"The money in the hands of the company in New York to be applied by it in the payment of interest, which by the terms of

[47]Railroad *v.* Jackson (1868) 74 U. S. 262; State Tax on Foreign Held Bonds (1872) 82 U. S. 300; Erie R. R. *v.* Pennsylvania (1894) 153 U. S. 628, 14 Sup. Ct. 952; Liverpool etc. Ins. Co. *v.* Board of Assessors (1899) 51 La. Ann. 1028, 25 So. 970, 45 L. R. A. 524.

[48]*Supra.*

[49]At p. 320.

[50]*Supra.*

the contract is payable in New York and not elsewhere, is property beyond the jurisdiction of Pennsylvania, and Pennsylvania is without power to say how the corporation holding such money, in another State, shall apply it, and to inflict a penalty upon it for not applying it as directed by its statutes."

CONCLUSIONS.

The fact that such sharp differences of opinion have existed among the learned justices of the Supreme Court and that the Treasury Department and the Attorney General now stand on record with diametrically opposing views is evidence that the questions presented are not free from difficulty.

The conclusions of the author, however, based upon this examination of the law, are as follows:

(1) Neither the Attorney General's opinion nor the Treasury Department's recent ruling is entirely correct. Under the present law, it is not proper to hold either that all income from stocks and bonds of corporations organized in the United States, owned by non-resident aliens, is taxable, nor to hold that all such income is not taxable.

(2) The law intends to tax all and only such income over which the United States has jurisdiction.

(3) The income tax is a tax on income and not a "direct" tax, except in a constitutional sense, and the ultimate test, therefore, where the United States has jurisdiction is not, even though the law purports to tax all income from "property in the United States", the location of the property out of which the income arises, but the location of the income as income.

(4) Where there are State statutes or decisions having the effect of creating a situs for stocks and bonds owned by non-resident aliens as property in the United States, and where the dividends and coupons are payable here, the income can be intercepted and taxed in this country, and is intended to be taxed by the income tax law.

(5) Where there is nothing to alter the logical rule that stocks and bonds owned by non-resident aliens have a situs only outside of the United States at the domicil of their owners, or where,

even though they have a situs here, the dividends or coupons are payable abroad, there is no income within the jurisdiction of the United States which can be reached, and such income is not taxable under the law.

(6) The present law should be amended to provide, if possible, a uniform rule, and to remove the present jurisdictional uncertainty in the matter.

AMOS J. PEASLEE.

NEW YORK CITY.